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OLC 75-0816/a

Approved For Release 2005/11/21 : CIA-RDP77M00144R000600120022-2

CENTRAL INTELLIGENCE AGENCY
WASHINGTON, D.C. 20505

2 May 1975

Mr. James F. C. Hyde
Acting Assistant Director for
Legislative Reference
Office of Management and Budget
Washington, D. C. 20503

Attention: Ms. Naomi R. Sweeney

Dear Ms. Sweeney:

This is in response to your request for the views of the Central Intelligence Agency on three alternate proposals to amend the formula for computing the cost-of-living adjustments to annuities under the Civil Service Retirement System. The proposals include a draft bill from OMB, a draft bill from the Civil Service Commission, and H.R. 3310, introduced by Representative David Henderson.

H.R. 3310, because of the two-month deadline for making cost-of-living changes, would be very difficult to implement and would create unnecessary hardships for employees in making timely decisions regarding retirement. Although many of the provisions of the OMB and Civil Service bills have similar purposes, CIA officials who deal with retirement matters prefer the draft bill prepared by the Civil Service Commission.

The Civil Service Commission draft would eliminate the one percent add-on bonus which is now part of the annuity formula. We believe this feature is an unreasonable windfall which adds dramatically to the drain of retirement funds, and we support its elimination.

The CSC bill would also provide that annuities should be adjusted downward whenever the Consumer Price Index (CPI) begins to decline. We support this idea, although with two stipulations. First, the apparent purpose of proposed section 8340(b) of Title 5 is to achieve uniformity with respect to the upward or downward revision of annuities. We believe the language of the parenthetical phrase (lines 13 and 14 of the bill) may not accomplish this, however, and suggest the following language be substituted "(calculated on the basis of the price index for the month of such three consecutive months as reflects the greatest change from the price index of the base month)." This would assure annuitants of the



highest level reached by the CPI for upward adjustments in annuities, and would assure the Government's interest in adjusting downward at the lowest level that the CPI reached during the three months.

Second, we believe that downward adjustments in annuities based on reduced cost-of-living should never result in an annuity below that which the annuitant has earned by operation of the general formula. As written, the bill would not only take away increases in annuities which have occurred because of rises in the cost of living, but also take away earned annuity. It is our view that the very least the annuitant should make is what his length of service and salary entitle him to by operation of the general formula.

Thank you for the opportunity to comment. I hope our views will prove to be of value to your office.

Sincerely,

[Redacted Signature]

George L. Cary
Legislative Counsel

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| <input type="text"/> <p>I drafted this letter on the three proposals to amend the cost-of-living annuity formula based on very helpful inputs from Personnel and Finance. Before we send it out we need your concurrence. Thanks.</p> <div style="text-align: right;"> <input type="text"/> Assistant Legislative Counsel </div> | | | |
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Attached are three proposals which would alter the present formula for determining cost-of-living adjustments in civil service retirement annuities. Letter (A) is a Civil Service Commission proposal; (B) is an alternative Administration proposal sponsored by OMB; and (C) is a bill introduced by Congressman Henderson, Chairman of the House Post Office and Civil Service Committee. OMB has sent these three proposals to us for comments and needs our response by April 25th. May I please have your views on these proposals by April 22nd. Thank you.

Assistant Legislative Counsel

cc:

OP

OF

DDA

Comptroller *Red 712 - No comment*

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EXECUTIVE OFFICE OF THE PRESIDENT

OFFICE OF MANAGEMENT AND BUDGET

WASHINGTON, D.C. 20503

APR 16 1975

LEGISLATIVE REFERRAL MEMORANDUM

To: Legislative Liaison Officer

Department of Defense
Department of State
Central Intelligence Agency ✓

Subject: (A) Civil Service Commission draft bill "To amend the formula for cost-of-living adjustments of annuities under the Civil Service Retirement System;"

10/16/75-0816
OP
of
C. S. R.

(B) H.R. 3310, "To amend title 5, United States Code, to revise the method of determining cost-of-living increases payable to civil service annuitants;"

(C) draft bill prepared by the Civil Service Commission at Office of Management and Budget staff request for consideration as a possible alternative.

The Office of Management and Budget would appreciate receiving the views of your agency on the above subject before advising on its relationship to the program of the President, in accordance with OMB Circular A-19.

(X) Special circumstances require priority treatment and accordingly your views are requested by c.o.b. April 25, 1975.

Questions should be referred to Hilda Schreiber (395-4650) or to Ralph N. Malvik (395-4702), the legislative analyst in this office.

Naomi R Sweeney

Naomi R. Sweeney, for
Assistant Director for
Legislative Reference

Enclosures



CHAIRMAN

Approved For Release 2005/11/21 : CIA-RDP77M00144R000600120022-2

UNITED STATES CIVIL SERVICE COMMISSION

WASHINGTON, D.C. 20415

April 15, 1975

Honorable James T. Lynn
Director, Office of Management and Budget
Executive Office of the President
Washington, D. C. 20503

Attention: Assistant Director for
Legislative Reference

Dear Mr. Lynn:

In keeping with the President's request that we restrain the overall growth of Federal expenditures and curb the rate of increase in the budget, we are attaching copies of letters by which the Commission proposes to submit to the Speaker of the House and the President of the Senate draft legislation (also attached) to amend the formula for cost-of-living adjustments under the Civil Service Retirement System.

This proposal, item number 94-27 of the Commission's 1975 Legislative Program, would modify the present formula by eliminating the extra 1 percent provision in the formula. We believe it should also apply to other Federal retirement systems (civilian and military) which now have the 1 percent add-on feature as part of their cost-of-living adjustment formula.

The proposal would eliminate the overcompensation which occurs over a period of time caused by the cumulative effect of the added 1 percent as used in the present formula and would (as described in the attached letters to the Congress) provide for a downward adjustment in annuities to correspond with a downward pattern in the CPI.

This proposal would reduce expenditures from the Retirement Fund, and would have a counter-inflationary impact. We estimate the savings from the CSC proposal (remove 1%) through 1979 would be as follows:

| <u>Fiscal Year</u> | <u>Savings</u> |
|--------------------|----------------|
| 1975 | — |
| 1976 | \$34 million |
| Transition quarter | 31 million |
| 1977 | 239 million |
| 1978 | 413 million |
| 1979 | 610 million |

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A number of alternative proposals are being developed by other agencies and H.R. 3310, which also modifies the present cost-of-living formula, has been introduced in the House by Representative Henderson. H.R. 3310 would eliminate the added 1 percent from the formula and adjust annuities on the first day of the second month which begins after the Consumer Price Index (CPI) has risen at least 3 percent above the point which triggered the last adjustment. H.R. 3310 also eliminates the requirement that the CPI stay 3 percent above the last base for two additional months.

While we agree with the thrust of H.R. 3310, its administration would be difficult because of the frequency of increases and the short time frame (only a few weeks) in which an increase would have to be implemented. For example, a rise of 3 percent in March, as indicated by the CPI published on or about April 22, would require a cost-of-living adjustment payable on June 1. Although H.R. 3310 would result in long-term savings similar to those under the recommended proposal, outlays in fiscal year 1976 would actually be increased because the first CPI adjustment would occur three months earlier than under the current formula.

STAT

We estimate that if H.R. 3310 is enacted, the increase or decrease in outlays through 1979 would be as follows:

| <u>Fiscal Year</u> | <u>Decrease</u> |
|--------------------|----------------------------|
| 1975 | (--) |
| 1976 | \$ (51) million (increase) |
| Transition quarter | (2) million (increase) |
| 1977 | 135 million |
| 1978 | 295 million |
| 1979 | 544 million |

Because H.R. 3310 would create very serious administrative problems and has no provision for the downward adjustment of annuities to correspond with a downward pattern in the CPI, and because any additional fiscal year 1976 expenditures are contrary to the President's program, we prefer the attached draft bill.

We will appreciate your informing us whether there is any objection to submission of the draft legislation as proposed.

By direction of the Commission:

Sincerely yours,

Chairman

Attachments



CHAIRMAN

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UNITED STATES CIVIL SERVICE COMMISSION

WASHINGTON, D.C. 20415

Honorable Carl Albert

Speaker of the House of Representatives

Dear Mr. Speaker:

I submit for the consideration of Congress, and recommend favorable action on, the attached draft bill to amend the formula for cost-of-living adjustments under the Civil Service Retirement System.

The current formula works in the following fashion. Civil Service Retirement annuities are adjusted on the first day of the third month that begins after the Consumer Price Index (CPI) has: (1) risen at least 3 percent above the point which triggered the last adjustment; and (2) remained at the higher level for 3 consecutive months. The annuity increase equals the highest percentage increase in the CPI during the 3-month period, plus 1 percent.

The Civil Service Retirement System is exceptional in respect to the extra 1 percent added to adjustments over and above the actual rise in the CPI. We know of no private employer, nor of any State or local governmental employer, that grants a similar added benefit, although the Foreign Service, Central Intelligence Agency, and military retirement systems share this feature with the Civil Service Retirement System.

A basic formula for making automatic cost-of-living adjustments has been a part of the Civil Service Retirement law since 1962. The 1 percent add-on feature did not appear until 1969, when it was enacted as part of P.L. 91-93.

The 1 percent add-on can have an overcompensating effect over a long period of time. This effect has been dramatically highlighted during the recent period of rapid inflation. For the first four years after this provision took effect, the Civil Service annuity adjustments occurred about once every 12 months. In the past 2 years, however, during a period of rapid inflation, increases have occurred every 6 months. With this degree of frequency, and with larger average increases, the 1 percent add-on builds up rapidly at a compound rate and becomes a serious problem.

The situation is illustrated by the fact that since November 1969 Civil Service Retirement annuity adjustments based on the CPI have increased by a total of 55 percent. Yet during this same interval, the CPI on which the adjustments were based has risen by a total of only 44 percent.

The financial magnitude of the situation is illustrated by the fact that the 55 percent annuity adjustment since November 1969 has added over \$20 billion to the unfunded liability of the Civil Service Retirement System. Of this amount, \$3.4 billion is attributable to the 1 percent add-on feature.

In terms of the future, the current adjustment provision will generate at least \$4 billion in additional unfunded liability for every 6 percent adjustment in annuities. About \$700 million of each \$4 billion amount is attributable to the 1 percent add-on. This relates to the current situation in that the average increase of the last 4 annuity adjustments has been 6 percent, and these increases have taken place at 6-month intervals.

To sum up, the provision for an additional 1 percent on each increase causes annuities to increasingly move ahead of the actual rise in cost of living, and is therefore undesirable and should be removed. Furthermore, it seems reasonable to include a provision for a downward adjustment of annuities to correspond with a downward pattern in the CPI. The draft bill contains a provision which would provide for such an adjustment on the first day of the third month that begins after the CPI has: (1) dropped at least 3 percent below the point which triggered the last adjustment; and (2) remained at the lower level for 3 consecutive months. In other words, the formulas for an increase or a decrease would be similar except for the upward or downward movement of the CPI.

This proposal for eliminating the 1 percent add-on would, if enacted, produce the following savings through 1979:

| <u>Fiscal Year</u> | <u>Savings</u> |
|--------------------|----------------|
| 1975 | -- |
| 1976 | \$ 34 million |
| Transition quarter | 31 million |
| 1977 | 239 million |
| 1978 | 413 million |
| 1979 | 610 million |

The Office of Management and Budget advises that from the standpoint of the Administration's program there is no objection to the submission of this proposal.

A similar letter is being sent to the President of the Senate.

By direction of the Commission:

Sincerely yours,

Chairman

To amend the formula for cost-of-living adjustments of annuities under the Civil Service Retirement System.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That title 5, United States Code, is amended as follows:

(1) Section 8331(16) is amended to read as follows:

"(16) 'base month' means the month for which the price index showed a percent change forming the basis for a cost-of-living annuity adjustment;"

(2) Section 8340(b)-(e) is amended to read as follows:

"(b) Each month the Commission shall determine the percent change in the price index. Effective the first day of the third month that begins after the price index change equals at least 3 percent for 3 consecutive months from the price index for the base month, each annuity payable from the Fund having a commencing date not later than that effective date shall be adjusted by the percent change in the price index (calculated on the highest level of the price index during the 3 consecutive months) adjusted to the nearest 1/10 of 1 percent.

(c) Applicability of an annuity adjustment under this section is governed by the commencing date of each annuity payable from the Fund as of the effective date of an adjustment, except as follows:

(1) An annuity (except a deferred annuity under section 8338 of this title or any other provision of law) which—

(A) is payable from the Fund to an employee or Member who retires, or to the widow or widower of a deceased employee or Member; and

(B) has a commencing date after the effective date of the then last preceding annuity adjustment under subsection (b)

1 of this section;
2 shall not be less than the annuity which would have been payable if
3 the commencing date of such annuity had been the effective date of
4 the then last preceding annuity adjustment under subsection (b) of
5 this section. In the administration of this paragraph, an employee
6 or a deceased employee shall be deemed, for the purposes of
7 section 8339(n) of this title, to have to his credit, on the
8 effective date of the then last preceding annuity adjustment under
9 subsection (b) of this section, a number of days of unused sick
10 leave equal to the number of days of unused sick leave to his
11 credit on the date of his separation from the service.

12 (2) Effective from its commencing date, an annuity payable from
13 the Fund to an annuitant's survivor (except a child entitled under
14 section 8341(e) of this title), which annuity commences the day
15 after the death of the annuitant and after the effective date of
16 the first adjustment under this section, shall be adjusted by the
17 total percent adjustment the annuitant was receiving under this
18 section at death. However, the adjustment in a survivor annuity
19 authorized by section 8 of the Act of May 29, 1930, as amended to
20 July 6, 1950, shall be computed as if the annuity commencing date
21 had been the effective date of the first increase under this
22 section.

23 (3) For the purpose of computing the annuity of a child under
24 section 8341(e) of this title that commences on or after the first
25 day of the first month that begins on or after October 20, 1969,

1 the items \$900, \$1,080, \$2,700, and \$3,240 appearing in section
2 8341(e) of this title shall be adjusted by the total percent
3 adjustments allowed and in force under this section on or after
4 such day and, in case of a deceased annuitant, the items 60 per-
5 cent and 75 percent appearing in section 8341(e) of this title
6 shall be adjusted by the total percent adjustments allowed and
7 in force to the annuitant under this section on or after such
8 day.

9 (d) This section does not authorize an adjustment in an additional
10 annuity purchased at retirement by voluntary contributions.

11 (e) The monthly installment of annuity after adjustment under this
12 section shall be fixed at the nearest dollar. However, the monthly
13 installment shall after adjustment reflect a change of at least \$1."

C

Dear Mr. Speaker:

I submit for the consideration of Congress, and recommend favorable action on, the attached draft bill to amend the formula for cost-of-living adjustments under the Civil Service Retirement System.

The current formula works in the following fashion. Civil Service Retirement annuities are adjusted on the first day of the third month that begins after the Consumer Price Index (CPI) has: (1) risen at least 3 percent above the point which triggered the last adjustment; and (2) remained at the higher level for 3 consecutive months. The annuity increase equals the highest percentage increase in the CPI during the 3-month period, plus 1 percent.

Provisions for automatically adjusting annuities or pensions in direct relationship to changes in the CPI are relatively uncommon, particularly in the private sector. Public sector retirement systems more typically make some provision for systematic cost-of-living adjustments. However, employers who make annuity adjustments commonly apply limitations on the amount and frequency of increases.

In relationship to the practices of retirement systems sponsored by most other employers, the Civil Service Retirement System is clearly more liberal in respect to its guarantee of automatic adjustments directly related to rises in the CPI. Furthermore, it is unique in respect to the extra 1 percent added to adjustments over and above the actual rise in the CPI. We know of no private employer, nor of any State or local governmental employer, that grants a similar added benefit, although the Foreign Service, Central Intelligence Agency, and military retirement systems share this feature with the Civil Service Retirement System.

A basic formula for making automatic cost-of-living adjustments has been a part of the Civil Service Retirement law since 1962. The 1 percent add-on feature did not appear until 1969 when it was enacted as part of P.L. 91-93.

The 1 percent add-on can have an overcompensating effect over a long period of time which has been dramatically highlighted during the recent period of rapid inflation. For the first four years after this provision took effect, the Civil Service annuity adjustments occurred about once every 12 months. In the past 2 years, however, during a period of rapid inflation, increases have occurred every 6 months. With this degree of frequency, and with larger average increases, the 1 percent add-on builds up rapidly at a compound rate and becomes a serious problem.

The situation is illustrated by the fact that since November 1969 Civil Service Retirement annuity adjustments based on the CPI have increased by a total of 55 percent. Yet the CPI on which the adjustments were based has risen by a total of only 44 percent. We believe it is also significant to note that in the period from July 1969 through October 1974, General Schedule salaries have risen by a total of only 38 percent.

The financial magnitude of the situation is illustrated by the fact that the 55 percent annuity adjustment since November 1969 has added over \$20 billion to the unfunded liability of the Civil Service Retirement System. Of this amount, \$3.4 billion is attributable to the 1 percent add-on feature.

In terms of the future, the current adjustment provision will generate at least \$4 billion in additional unfunded liability for every 6 percent adjustment in annuities. About \$700 million of each \$4 billion amount is attributable to the 1 percent add-on. This relates to the current situation in that the average increase of the last 4 annuity adjustments has been 6 percent, and these increases have taken place at 6 month intervals.

To sum up, the Civil Service Retirement System has a cost-of-living adjustment provision that is liberal in relation to retirement program provisions of other employers, even without considering the 1 percent add-on feature. From this perspective, the provision for an additional 1 percent on each increase, added in such a way as to increasingly move ahead of the actual rise in cost of living, becomes undesirable. The cost of this feature in the light of current economic conditions serves to intensify the degree to which its

desirability is being called into question. We believe that there are too many other more legitimate demands on scarce tax dollars to support further continuation of this costly provision.

At the same time, the practice of recognizing the inevitable lag between the time an increase is triggered and the time it can be placed in the hands of annuitants, by adding a small amount to the size of the increase, is worth retaining. Therefore, we are proposing a modification of the add-on procedure as provided in the attached draft bill. The modification will permit continued compensation to annuitants for the time it takes to effectuate an increase, a period during which the cost of living generally continues to rise. At the same time, the new procedure will avoid the past distortion between cumulative increases and rise in CPI by adding the 1 percent to the index used to trigger the next CPI increase.

This proposal would save money if enacted, and would have a counter-inflationary impact. We estimate the decreased outlay through 1979 would be as follows:

| <u>Fiscal Year</u> | <u>Decrease</u> |
|--------------------|-----------------|
| 1975 | - |
| 1976 | \$91 million |
| Transition quarter | 57 million |
| 1977 | 411 million |
| 1978 | 530 million |
| 1979 | 690 million |

A BILL

To amend the formula for cost-of-living adjustments of annuities under the Civil Service Retirement System.

1 Be it enacted by the Senate and House of Representatives of the United
2 States of America in Congress assembled, That title 5, United States
3 Code, is amended as follows:

4 (1) Section 3307(d) is amended by striking out "(20) and (21)" and
5 inserting "(21) and (22)" in place thereof.

6 (2) Section 8331 is amended--

7 (A) by renumbering subsections (17), (18), (19), (20), and
8 (21), as (18), (19), (20), (21), and (22) respectively; and

9 (B) by inserting after subsection (16) a new subsection (17)
10 as follows:

11 "(17) 'base index' means price index for the base month, increased
12 by 1 percent;".

13 (3) Section 8340(b) is amended to read as follows:

14 "(b) Each month the Commission shall determine the percent change in
15 the price index. Effective the first day of the third month that begins
16 after the price index change equals a rise of at least 3 percent for 3
17 consecutive months over the base index, each annuity payable from the Fund
18 having a commencing date not later than that effective date shall be in-
19 creased by 1 percent plus the percent rise in the price index (calculated
20 as the percentage difference between the highest level of the price index
21 during the 3 consecutive months and the base index) adjusted to the nearest
2 1/10 of 1 percent."

B

94TH CONGRESS
1ST SESSION

H. R. 3310

IN THE HOUSE OF REPRESENTATIVES

FEBRUARY 19, 1975

Mr. HENDERSON introduced the following bill; which was referred to the Committee on Post Office and Civil Service

A BILL

To amend title 5, United States Code, to revise the method of determining cost-of-living increases payable to civil service annuitants.

1 *Be it enacted by the Senate and House of Representa-*
2 *tives of the United States of America in Congress assembled,*
3 That section 8340 (b) of title 5, United States Code, is
4 amended to read as follows:

5 “(b) Each month the Commission shall determine the
6 percent change in the price index. Effective the first day
7 of the second month that begins after the price index change
8 equals a rise of at least 3 per centum for a month over the
9 price index for the base month, each annuity payable from

1 effective date shall be increased by the percent rise in the
2 price index adjusted to the nearest 1/10 of 1 percent."

3 SEC. 2. (a) Except as provided in subsection (b) of this
4 section, the amendment made by the first section of this Act
5 shall become effective on the date of enactment of this Act.

6 (b) In the event the price index change, as determined
7 by the Civil Service Commission under section 8340 of title
8 5, United States Code, for the month during which this pro-
9 vision is enacted, equals a rise of at least 3 per centum over
10 the price index for the base month currently in effect under
11 such section 8340, each annuity payable from the Civil
12 Service Retirement and Disability Fund shall be increased,
13 effective on the first day of the second month that begins
14 after the date of enactment of this Act, by the per centum
15 rise in the price index adjusted to the nearest 1/10 of 1 per
16 centum.